

This record is a partial extract of the original cable. The full text of the original cable is not available.

C O N F I D E N T I A L SECTION 01 OF 02 YEREVAN 002769

SIPDIS

STATE FOR EUR/CACEN, EUR/ACE, EB

E.O. 12958: DECL: 12/14/2014

TAGS: ECON ENRG AM RS

SUBJECT: RUSSIAN POWER GIANT MOVES TO CONSOLIDATE CONTROL
OVER ARMENIA'S ENERGY SECTOR

REF: A) 03 YEREVAN 2023 B) 03 KIEV 4530 C) 02 YEREVAN

2093

Classified By: A/DCM Larry Richter for reasons 1.4 (b/d)

SUMMARY

¶1. (C) Russian energy giant RAO-UES is moving to take over Armenia's sole electricity distributor, Electricity Networks of Armenia (ElNetArm), which would consolidate its hold on Armenia's energy infrastructure. The director of ElNetArm and officials in the Government of Armenia have acknowledged the possibility of a sale to RAO-UES and at the same time expressed reservations about a sale to any Russian company, and especially to RAO-UES, on the grounds that it will lead to Russian vertical domination of the Armenian power sector. RAO-UES already controls 80 percent of Armenia's power generation capacity and the distribution network in Armenia's main export market, Georgia. Iosif Isayan, Deputy Minister of Energy, told us that the Minister of Energy opposes the deal and will consider ways to block it. The Minister of Justice told us he thought the deal was "dangerous" and would create a system that is "impossible to regulate." Apart from concerns about market regulation, consolidated Russian control of distribution is a step backwards from Armenia's stated energy policy goal of reducing Russia's control over its energy infrastructure. End Summary.

ElNetArm FOR SALE

¶2. (C) Yevgeniy Gladunchik, ElNetArm's Director General, told PA Consulting, a USAID implementer in the energy sector, (and a member of ElNetArm's staff confirmed to us) that ElNetArm's owners were looking to sell the distribution company as soon as possible. Gladunchik was called to Moscow to meet with the owners, who were visiting a steel factory they own there. (Note: ElNetArm is owned by Midland Resources, an offshore British company whose primary shareholder is Ukrainian oligarch Eduard Shifrin (ref B). Armenian oligarch and National Assembly Member Harutiun Pambukian is also a stakeholder in Midland. End Note.) Gladunchik was told to provide the 2004 financial statement of the company as soon as possible so that they could offer the company for sale. They intend to sell the company in order to free up assets for another acquisition. According to Gladunchik, Midland Resources hopes to get USD 100 million for the company.

RUSSIA BUYING

¶3. (C) According to Gladunchik, three firms have expressed an interest in purchasing ElNetArm: RAO-UES, Energotech Export, and another, unnamed Russian firm. In a December 15 meeting, Minister of Justice David Harutyunian volunteered that there has been discussion about RAO-UES buying the company, although he (correctly) emphasized that this was a private commercial deal and that the government was not involved except to approve or disapprove of the deal once it had been formally offered. In a December 16 meeting with the Ambassador, AmCit Director of the Diaspora Armenia Cafesjian Foundation, John Waters, told us that he had approached Midland stakeholder and National Assembly member Harutiun Pambukian to try and buy the company in an effort to block further Russian domination of the energy sector. Waters told us that Midland Resources and RAO-UES were planning to sign a letter of Intent to Sell in the "very near future." Publicly, both RAO-UES and ElNetArm have recently denied press reports about an imminent sale following the November 30 meeting of RAO-UES Management Board Chairman Alexander Voloshin with President Kocharyan and Gladunchik.

¶4. (U) RAO-UES's acquisition of the distribution network would leave only two major energy assets outside of RAO-UES's control, the Vorotan Cascade Hydro-Power Plant (controlled by the Armenian government) and the Yerevan Thermal Power Plant. In the last two years, RAO-UES took financial control of the

Armenia Nuclear Power Plant (ANPP), five hydro-electric power plants in the Sevan-Hrazdan Cascade, and the Hrazdan thermal power plant (ref A). RAO-UES controls 80 percent of Armenia's electricity generation capacity, as well as the distributor in Armenia's single paying export market, Georgia. In addition, Russian state-controlled firm Gazprom owns a majority share of ArmRosGazprom, which controls the delivery of all piped natural gas in Armenia, and Russian firms control the supply of the nuclear fuel for the Armenia Nuclear Power Plant.

REGULATORY APPROVAL REQUIRED

15. (SBU) Acquisition of the distribution company requires the approval of the Public Services Regulatory Commission (PSRC).

In a December 15 meeting, Minister of Justice David Harutyunian (who struck the original privatization deal with Midland Resources) volunteered that he knew about the proposed sale to RAO-UES, but that he was "not sure" if there would be a deal, and that a sale to RAO-UES would be "dangerous" because they would be difficult to regulate as both distributor and generator. He added that the deal he had struck with Midland Resources two years ago had many "poison pills" in it that, in effect, required the approval of the GOAM to sell the company. Iosif Isayan, Deputy Minister of Energy, told us the Minister of Energy was concerned about the sale and that the Ministry was considering how to block it. (Note: The original sale to Midland Resources was not transparent. Midland's stakeholders are well connected in Armenia and Russia and may be able to influence government officials (ref C). End Note.)

AMERICAN DIASPORA GROUP INTERESTED

16. (SBU) The Cafesjian Foundation, owned by AmCit Diaspora Armenian Gerard Cafesjian, is seeking to bid on ElNetArm in order to avoid Russian domination of the energy sector. In a December 16 meeting with the Ambassador, Cafesjian's new director John Waters told the Ambassador that he was looking for partners to participate in the bid, but that Cafesjian could, if necessary, finance an investment of USD 75 to 100 million himself. Waters said that he had approached Richard Stanaro of EBRD, who said that EBRD would be willing to participate and put up 35 percent. Cafesjian bid on ElNetArm three years ago with financing from EBRD, but the GOAM ultimately rejected their bid in favor of Midland Resources. Waters told us that he was trying to get the deal together very quickly, as he understood that RAO-UES and the government of Armenia are to sign a letter of Intent to Sell very soon. Comment: American investment in ElNetArm would be an important step towards Armenia's goal of reducing its energy dependence on Russia. Cafesjian is likely the best candidate for the job, because he is policy minded and can afford to suffer some financial loss (although ElNetArm was officially Armenia's most profitable company in 2004). Nevertheless, Midland Resources is a private company, so there is no place for our advocacy on Cafesjian's behalf. End comment.

COMMENT: SLOUCHING TOWARDS MOSCOW?

17. (C) Russian firm RAO-UES currently dominates Armenia's electricity generation capacity: Armenia should have a strong interest in keeping Russian firms, especially RAO-UES, out of its distribution network. If RAO-UES is successful in its bid to buy ElNetArm, a single company will serve as the primary generator, sole distributor (and, therefore, exporter) and foreign client of Armenian electricity. It would be a difficult regulatory task to prevent the export of Armenia's cheapest electricity at market prices while charging Armenian consumers tariffs for more expensive generation. Besides this market concern, further Russian control goes against the Government of Armenia's stated energy policy of freeing itself from heavy energy dependence on a single state or actor. While the Government has no legal authority to demand how a purchaser is selected, it does have the authority to approve or disapprove the purchase. The approval of a sale to RAO-UES would be hard to explain in terms of Armenia's interest in its energy market or its concerns about energy dependence.

EVANS